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Current Support Brief

SHIFTS IN EGYPTIAN ECONOMIC POLICY

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SHIFTS IN EGYPTIAN ECONOMIC POLICY

Economic realities apparently are forcing Egypt to modify longstanding policies aimed at improving living standards while keeping prices and taxes at the lowest possible levels. Although actual changes made to date have been slight, budget data, along with various press articles, indicate that more extensive adjustments are programed and probably will be enacted in the next few months. The slight alterations of direction presently discernible are being taken reluctantly in response to severe strains in the Egyptian economy, and the pattern of change appears to conform, at least in part, to recommendations of international lending institutions. Although recent moves may be intended merely as stopgap measures, in the absence of overriding domestic political repercussions long-range requirements for foreign assistance could make these changes self-perpetuating.

1. Past Policies on Consumption

The economic policy of Egypt consistently has postulated greatly increased personal incomes concurrent with price stability. With 1960 as a base year, the cost-of-living index stood at 97 in January 1963 and the wholesale price index at 101. Per capita production, which rose by about 5 percent between 1960 and 1962, was about $150 in mid-1962, whereas per capita expenditures -- consumption plus investment -- were between $155 and $160. Prices have been restrained and the gap has been bridged by dipping into the foreign exchange till and by government borrowing on domestic account.

The annual deficit expenditure of from $5 to $10 per capita has resulted in a serious strain on national financial resources (see the charts*). From 1959 through the middle of 1962, net resources used to finance the foreign trade deficit on current account were about $720 million, and the foreign trade deficit for 1963 may run as high as $330 million. As a result, foreign exchange reserves have been nearly exhausted and foreign borrowing has sharply increased. Price stabilization, in the face of the trade imbalance and the growing consumer demand, has been accomplished through a complicated system of subsidies for consumer goods, with the government making up the difference between retail prices and production or acquisition costs. Prices on both imported and domestic goods have been fixed by the

* Following p. 5.

government, and unrealistically low prices in both categories have had an adverse effect on the balance of payments. Subsidies on imported commodities and low prices on goods containing imported components have stimulated demand for imports, whereas low prices for domestic products have encouraged home consumption at the expense of exports. The cost of these subsidies also has contributed to recurring deficits in the domestic budget.

Because of its interest in raising living standards, the government has been extremely reluctant to raise taxes to a level sufficient to balance the budget. As a proportion of national income, tax revenues actually have declined from 15.6 percent in fiscal year 1958 to 13.7 percent in the fiscal year ending 30 June 1962. Ordinary budget expenditures during this period have risen 40 percent, but tax receipts have increased only 14 percent. The added tax revenues have come almost entirely from import and excise duties. Spendable personal income has been maintained at as high a level as possible by keeping income and property taxes almost unchanged.

2. Signs of Change in Consumption Policy

Whereas government expenditures on subsidies for consumer goods have grown rapidly, from 9 million Egyptian pounds* for fiscal year 1961 to 36.5 million for fiscal year 1963, the budget for the current year shows a decrease to 32.4 million Egyptian pounds in this allocation. The long-standing policy of price stabilization has been breached by recent increases in the prices of sugar and electricity. The government has gone to great lengths to justify these increases to the population and obviously finds such action distasteful. In light of the budget data on subsidies, these price increases suggest that the regime, however reluctantly, is relaxing one of its most cherished economic principles.

Articles in the government-controlled press similarly are suggestive of new policies. In August the semiofficial newspaper Al-Ahram ran a lengthy series in four parts heavily underscoring the economic drain caused by large personal consumption expenditures. According to the author, consumer imports in 1962 were about $100 million greater than in 1961. The articles laid great stress on the recently increased material welfare of Egyptian citizens and then reiterated many times the necessity of sacrificing some other current consumption gains. The reader was exhorted to understand that imports must be cut and that consumption of

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* The current rate of exchange for the Egyptian pound is US $2.30 to 1 Egyptian pound. This is a new rate as of early 1962.

domestic products must be reduced so that these goods could be sold abroad.

This public airing of the problem was followed by a period of quiet, probably resulting from extreme official and press preoccupation with affairs in Yemen, the Algerian-Moroccan dispute, and political developments in Iraq and Syria. In November, however, the government news agency began releasing small items that tend to confirm the existence of new policies. On 11 November a member of the Presidential Council, reporting to a government-sponsored Administrative Development Conference, stated that credit facilities and foreign currency should be allotted to Egyptian private businessmen so that they could contribute their share to the building of the "Arab socialist society." The official also reported that public information media are to be utilized to make all citizens fully aware of the "social and national responsibilities." Three days later this same conference issued resolutions incorporating the above suggestions and urging that national development projects be financed by "compulsory savings through such media as social insurance and raising the prices of luxury commodities." In the context of Nasser's methods of operation, the series of articles in Al-Ahram and the conference report appear to presage even stricter import controls, relaxation of price controls on imported items and on domestic products suitable for export, and enactment of some form of social security tax to supplement government revenues.

The budget for the current fiscal year similarly points to a forthcoming alteration in the tax structure, although only slight changes have been announced to date. The new budget calls for a 5.5-percent increase in government revenues for fiscal year 1964 -- total tax yields are to increase 11.6 percent, and the income and property tax receipt category shows a jump of 18.5 percent. Although actual revenues and expenditures often vary greatly from Egyptian budgets, the magnitude of the relative changes is evidence that increased income and property taxes probably are to be imposed.

3. Recommendations of the International Lending Agencies

Egyptian authorities are projecting a deficit in the balance of payments of about $230 million in the fiscal year ending 30 June 1964, and this understates the probable deficit by as much as $100 million. Foreign currency reserves as of the end of 1963 are less than $15 million and Western commercial banks are exceedingly reluctant to renew outstanding credit lines for more than 1 or 2 months at a time. To

cover the imbalance, therefore, the government of Egypt anxiously has been seeking loans from the International Monetary Fund (IMF), the International Bank for Reconstruction and Development, the US, the UK, and other potential sources. All of these Western sources have insisted on alterations in Egyptian economic policy, and the evidence of impending changes should be considered in light of the following program outlined by the IMF as prerequisite to further loans:

a. Introduction of additional taxes*
b. Adjustment of the exchange rate system
c. Uniform application of higher discount rate by the Central Bank
d. Reduction of cost of living subsidies*
e. Revision of price structures in industry, power, and transport*
f. Establishment of ceilings on credit expansion
g. Lifting export quotas and removal of price controls on agricultural products
h. Relaxation of foreign trade and payment restrictions

4. Motivation for Change

The apparent shifts in economic tactics undoubtedly arise primarily from Egypt's desperate need for outside assistance, particularly in the form of foreign exchange. Western solidarity in urging changes along the lines recommended by the IMF has been complete, and Egypt may be trying to adopt the minimum measures necessary to get money from these sources. Shortages of foreign currency in past periods have contributed to a noticeable shortage of consumer goods, and such shortages probably are reinforcing the nascent program aimed at cutting domestic consumption.

Given such motives, the responsible Egyptian authorities probably intend taking only minimum and temporary steps to elicit an adequate in-flow of foreign capital. A brief bow to international financial pressures, however, is not likely to suffice. Rapid industrialization, huge foreign trade deficits, and compensation to foreign owners of nationalized firms all will require sizable injections of foreign funds for many years to come. Inasmuch as the Soviet Bloc has shown no disposition to commit sums of the necessary magnitude, the funds can come only from international lending agencies and Western governmental and

* There is evidence of adoption of these measures by the Egyptian authorities.

private organizations. Continuing evidence of more realistic internal economic planning will be prerequisite to governmental loans, and private entities will not risk large sums without some confidence that Egypt is developing a more viable economy with an ability to meet payments when they are due. Egyptian self-interest, therefore, appears to dictate continued adherence to some aspects of the IMF strictures and resulting deviation from those economic policies considered most damaging to the Egyptian economy by Western financial experts. Should the first steps toward higher prices and taxes create strong domestic political reactions, political expediencies may restrict implementation of such new policies and minimize any impact, but only at the expense of reducing the availability of external economic assistance and recent levels of economic growth.

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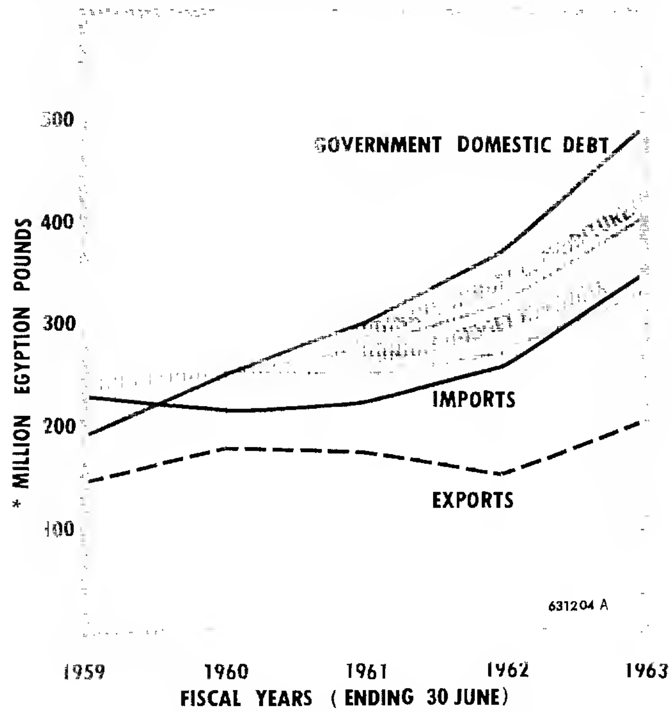
EGYPT'S DEVELOPING DOMESTIC DEBT



* The Egyption pound is currently valued at $2.30

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